

**UPDATE
ON QUÉBEC'S
ECONOMIC AND FINANCIAL
SITUATION**

**A MESSAGE
FROM THE MINISTER OF FINANCE**

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November 4, 2008



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A Message from the Minister of Finance

The financial crisis spawned in the United States is spreading to every continent and foreshadows a severe global economic slowdown. However, thanks to disciplined management of public spending over the last five years and the steps the government has taken to support employment, Québec is in a favourable position to deal with the slowdown.

The scale of this financial crisis is such that it has led to the failure of major financial institutions, a tightening of bank credit and a sharp decline on stock markets.

To mitigate the effects of tighter credit, the central banks of the industrialized countries have taken exceptional measures. They have coordinated a substantial drop in their leading interest rates and have injected massive amounts of liquidity into the financial system.

This financial crisis is now affecting the real economy, slowing investment, international trade, consumption and employment in many regions of the world.

In fact, growth in the industrialized countries will fall sharply this year and next. From 2% to 3% in 2007, it will decline to about 1% this year and less than 1% in 2009.

Québec is one of the most open economies of the world. Exports account for 50% of our gross domestic product and 75% of our international exports are sent to the United States. Accordingly, Québec is directly affected by the economic slowdown.

We cannot avoid the global economic slowdown. However, we can prepare for it. We have to act to reduce its consequences.

That is what our government has been doing since 2003.

We have managed our public finances with discipline and prudence over the last five years.

We have also supported employment and investment, and protected Quebecers' purchasing power.

Québec has never been this well prepared to face an economic slowdown.

Our disciplined management of public spending, combined with the very good performance of Québec's economy, have allowed us greater leeway as the economic slowdown approaches.

- I am announcing that the Québec government achieved an additional budgetary surplus of \$484 million during fiscal year 2007-2008.

This is the result of our discipline, the Premier's leadership and my colleagues' teamwork.

It reflects disciplined control of spending. Since 2003, our government has kept the average annual growth rate in program spending at 4.5% compared with 6.5% on average for the Canadian provinces.

It also reflects Québec's good economic performance, stimulated in particular by tax cuts, the pay equity settlement, the implementation of our plan to repair our infrastructures and measures to encourage our businesses to invest.

Today, we are well prepared to face the economic slowdown.

The surplus achieved in 2007-2008 is in addition to the \$1.8 billion reserve constituted as a measure of prudence in the last budget.

With a reserve of \$2.3 billion, including a contingency reserve of \$200 million we have yet to use, Québec is well prepared to face a downturn.

- Thanks to this reserve, I can announce that Québec's public finances will remain balanced this year and next.

Keeping the budget balanced will continue to demand disciplined management of program spending. Still, our good management now allows us, compared to the *2008-2009 Budget*, to raise spending growth to 4.4% in 2008-2009 and to 3.2% in 2009-2010.

Our government has been vigilant. From the initial signs of the slowdown, we acted with determination to support employment and protect Quebecers' purchasing power.

- To support employment in all the regions, we invested massively in public infrastructures and energy development. In 2008, these investments reach \$12.4 billion, including almost \$8 billion in infrastructures and \$4.5 billion in energy development. Investments in each of 2009 and 2010 will amount to \$13.5 billion.

To understand the importance of these investments in Québec's economy, it is useful to note that \$1 billion of investment in infrastructure leads to the creation of 8 000 direct jobs. By way of comparison, between 1998 and 2003, the government's annual public investments averaged \$2.5 billion. Under our government, annual public investment in Québec's economy has therefore tripled.

The government will step up the pace of investment in public infrastructure to further support employment. At the last meeting of the Council of the Federation last month in Montréal, all the provincial governments undertook to accelerate their investments in public infrastructure.

- To protect Quebecers' purchasing power, we have cut taxes by more than \$1 billion. This tax cut represents, for a family, a gain of up to \$2 000.
- To support workers, the government has implemented the Employment Pact. That is an investment of \$1 billion over three years, in partnership with the private sector, in worker training, acquisition of new skills, support for social assistance recipients who want to return to work, and in the hiring of newcomers.
- To support our businesses, we have eliminated the capital tax for the manufacturing sector and introduced an investment tax credit. Overall, businesses benefit from tax relief totalling \$880 million in 2008-2009 and \$1.2 billion in 2009-2010.
- To help sectors in difficulty meet the challenge of strong international competition, the government has implemented action plans totalling more than \$2 billion:
 - the four-year, \$621-million Action Plan for the Manufacturing Sector;

- the support plan for the forest sector, with \$1.4 billion over five years;
 - the three-year, \$82-million strategy for Québec's clothing and fashion industry.
- In addition, we have allocated almost \$900 million over three years to the Québec Research and Innovation Strategy.

Economists have hailed our plan.

The Mouvement Desjardins, the National Bank and the Royal Bank estimate that our government's plan is contributing to keeping Québec's economy growing. Indeed, Québec's plan has been followed: for instance, British Columbia and Saskatchewan have also cut taxes and increased public investments.

When the world's largest economy stumbles at our front door, our house cannot escape being shaken. Despite that, we believe that Quebecers' talent and know-how, together with our government's determination, should allow growth to continue.

- Accordingly, we are forecasting economic growth in Québec of 0.8% in 2008 and 0.6% in 2009.

Most private sector economists expect economic recovery by the beginning of 2010.

Our disciplined management has provided us with leeway that we can now apply to implement new targeted measures to further support our economy and Quebecers purchasing power.

These measures were not prepared in isolation. They are based on sustained discussions between our government and our economic partners.

Last October 8, the Premier announced the formation of three teams to closely monitor employment, economic activity and financial markets.

Many meetings were held and our government's action has drawn inspiration from them.

New measures will be introduced on January 1, 2009 to protect Quebecers' standard of living and support families' consumption.

- I am announcing that the indexing rate of fiscal parameters for 2009 will be 2.36% rather than 1.58% as stipulated in the *2008-2009 Budget*. That means \$136 million more to support Quebecers' purchasing power.
- For seniors, I am announcing that the amount eligible for the tax credit for retirement income will rise from \$1 500 to \$2 000. That is \$47 million more for 350 000 retired households.

- Social solidarity benefits will also be indexed at 2.36%. In addition, I am announcing that the benefits of recipients fit for work will henceforth also be fully indexed. That means \$66 million more for 332 000 households.

The Québec government has also approached the federal government to have changes made to certain rules.

- Accordingly, we have asked the federal government to set the age limit at which a saver is required to dip into his registered retirement savings funds at 73 rather than 71. These additional two years would provide more time for savers concerned to benefit from a recovery in the markets.
- Also, to support the purchasing power of young families and support the housing market, we have asked for the deferral, without penalty, of the 2009 repayment of a loan made from a registered retirement savings plan to purchase a home, what is commonly called an HBP (Home Buyers Plan). This would make an additional \$300 million of cash resources available to 382 000 Québec households.

We are also introducing new measures to help businesses face a possible tightening of credit.

- I am announcing a special program of loans and loan guarantees allowing businesses to have access to additional financing of \$1 billion. Investissement Québec will administer the program.

Under this program, the government will guarantee the loans made to a business to support its working capital or make strategic investments.

Moreover, the fall in the stock market will have an impact on supplemental pension plans.

To deal with this difficult situation, the government will work to ensure the solvency of plans, while taking the financial situation of companies into account, as well as the interests of workers and pensioners. To achieve this objective, the government intends to involve employers, unions and pensioners.

A temporary deterioration in the financial situation of these plans must not be allowed to affect the companies, workers and ultimately the pensioners.

To that end, the Minister of Employment and Social Solidarity will unveil a series of measures in the near future targeting defined-benefit supplemental pension plans. These include:

- setting up task forces formed of representatives of employers, unions and municipalities mandated to come up with possible solutions;
- applying standards for pension plans facing particular situations. For instance, the solvency deficiency amortization period could be lengthened (e.g.: from five to ten years);

- undertaking to apply, effective December 31, 2008, the actuarial standards the Canadian Institute of Actuaries plans to bring into force in 2009, as long as they result in reducing the deficits of pension plans.

These targeted measures are in addition to the tax cuts, investments in public infrastructure and the measures to support workers and businesses to enable Québec to get through this period of turbulence with confidence.

The government is also concerned to prepare Québec for the economic recovery expected by early 2010.

Our government is implementing a vision of Québec's economic future that will accelerate and intensify the recovery. For more than a year, the Premier has begun to build a new economic space with all Québec. Construction of this new space is well underway.

During President Sarkozy's visit to Québec City, Québec and France signed an agreement, the first of its kind in the world, on the recognition of prior learning and skills. This agreement will enable a trained worker from one side of the Atlantic to practise his trade on the other side. That is part of the answer to one of Québec's greatest economic challenges: the lack of manpower.

At the time of this visit, the Canada – European Union Summit also took place during which a crucial step was taken towards formal negotiations on a next-generation transatlantic agreement between Europe and Canada. Québec's leadership is behind this historic rapprochement between two continents.

Another project is the negotiation of an economic partnership with Ontario to remove obstacles that hamper trade.

Québec has also convinced its partners on the Council of the Federation to implement, by next spring, a pan-Canadian agreement on labour mobility. Under this agreement, a qualified worker will be able to apply for a job anywhere in the country.

The Premier also unveiled his intention to initiate a new phase of development of Québec's North to, among other things, develop our immense mining, energy and tourism potential. The development of our natural resources, in particular hydroelectricity, is a pledge of collective wealth for decades to come.

Taken together, these five components of the new economic space – the France-Québec agreement, the agreement with Europe, a trade agreement with Ontario, pan-Canadian labour mobility and the Plan Nord – constitute a genuine repositioning of Québec.

To prepare Québec for the economic recovery expected in early 2010, the government also intends to continue and intensify its efforts to improve worker training in order to deal with the scarcity of qualified labour that hampers economic development, particularly in the regions.

We will also continue and intensify our efforts to stimulate business investment, innovation and new business start-ups in future-oriented sectors. To do so, in particular, we will foster a competitive corporate and personal tax system.

From the first signs of recovery, our economy will be well prepared and on the road to sustainable economic growth that will secure Québec's prosperity for a generation.

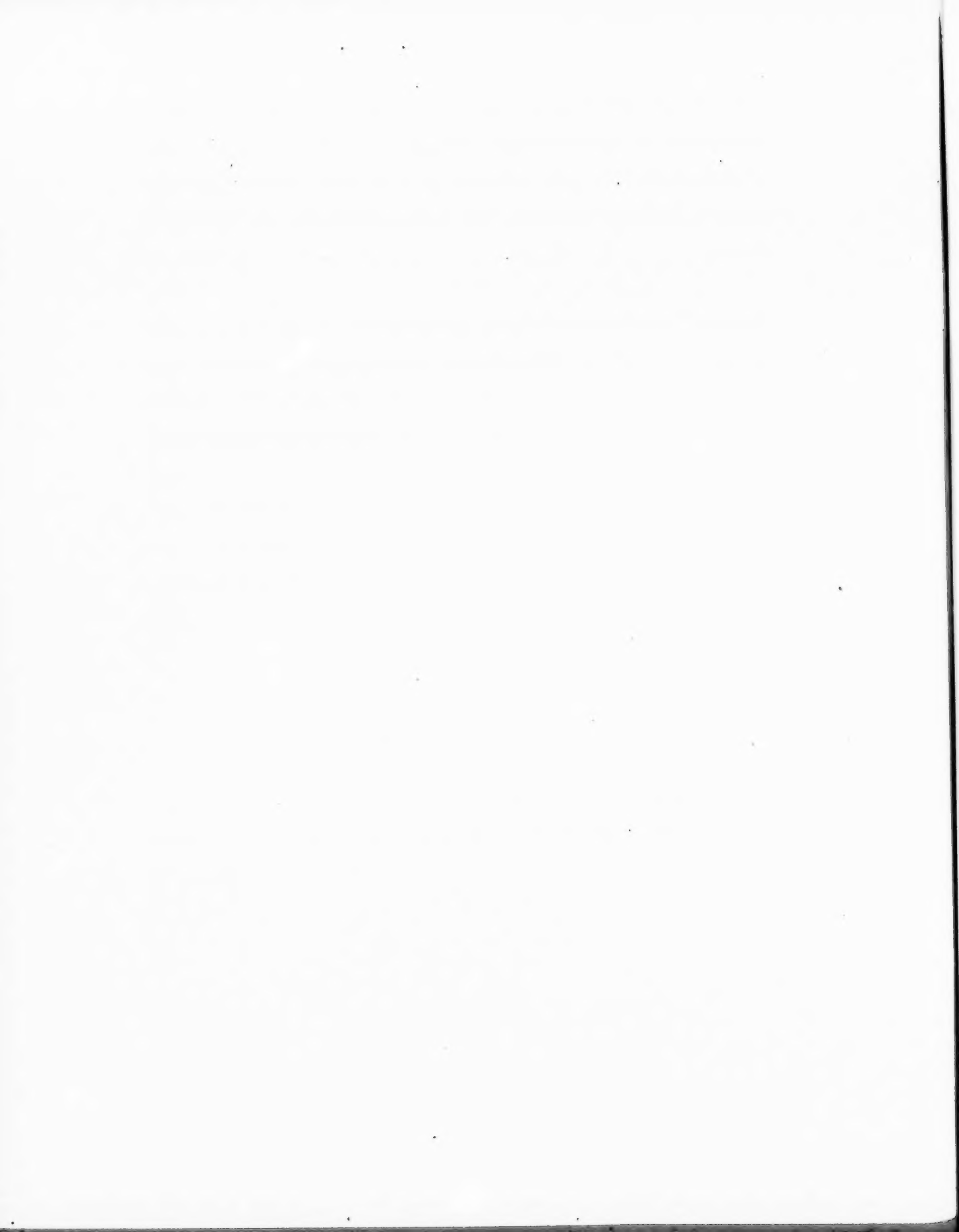
This is not the first time Québec has faced an economic slowdown.

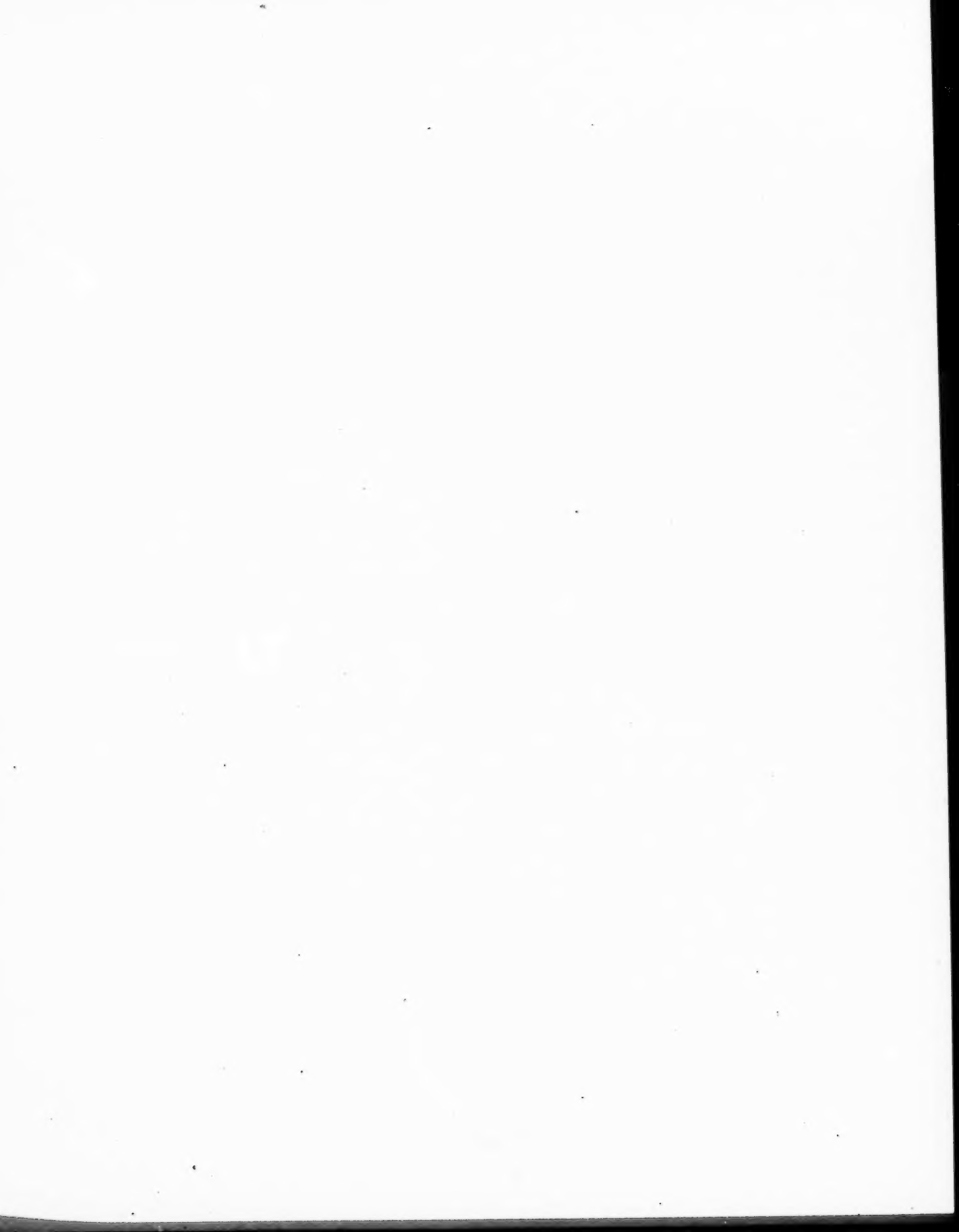
However, thanks to our prudent and disciplined management, Québec has never been so well prepared to deal with economic turbulence.

We will keep the budget balanced, support families' purchasing power, protect Quebecers' jobs, mitigate the effects of tighter credit on businesses and accelerate the pace of public investments that generate economic activity, wealth and employment in every region of Québec.

Thanks to our economic vision, our discipline and our rigor, we will be among the first on the starting line when better times return.

We have every reason to look ahead to Québec's economic future with confidence and optimism.





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